

If You Haven't Filed Your Prior Tax Returns; This Might Be the Best Time To Do So!

Related Professionals

Paul G. Topolka
336.387.5123
ptopolka@nexsenpruet.com

David M. McCallum
919.573.7440
dmccallum@nexsenpruet.com

Practices

Tax Law

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At various points in time, the IRS offers “initiatives” to assist businesses and individuals with various tax issues. Most often these initiatives offer favorable terms or inducements to a class of taxpayers with respect to conduct that conforms to the spirit of the initiative – for example, accepting an IRS offer to administratively settle a tax matter rather than litigate. Recently, and due to the COVID-19 pandemic, the IRS announced on March 25 in IR-2020-59 (dubbed “People First Initiative”), a series of relief measures for taxpayers facing various challenges posed by the pandemic. One of the topics addressed in this initiative was “Non-filers.”

The IRS encouraged individuals who have not filed returns during the last three years (2016, 2017 and 2018) to file their delinquent returns now. The IRS noted that more than **one million households** have not filed their returns in the last three years and that some of those taxpayers are actually owed refunds. For the 2016 year, any refund due will now expire on July 15, 2020, so the return (Form 1040) must be filed on or before that date or otherwise, your refund becomes the property of the U.S. Treasury. Once the delinquent returns are filed, the taxpayers with tax liabilities should consider taking the opportunity to resolve any outstanding liabilities if full payment is not an option by entering into an Installment Agreement or an Offer in Compromise with the IRS to obtain a “Fresh Start.” The suspension period, which lasts until July 15, offers a further opportunity to become compliant with a non-filer’s tax obligations. Also worthy of note is that 2020, with likely **reduced** income due to current economic conditions, will become the base year for any Offer in Compromise once the non-filer is in the program.

Prior to this initiative, the IRS had previously announced on February 19 (IR-2020-34) that it will begin visits to high-income taxpayers who haven’t filed tax returns. High-income non-filers are those who generally received income in excess of \$100,000 during a tax year and did not file a tax return with the IRS. Soon, revenue officers from the IRS will be knocking on doors of those high-income non-filers or contacting them with planned visits – denominated by the IRS as “HINF” cases.

But why should a non-filer file delinquent tax returns if he/she hasn't received a notice or letter from the IRS and therefore, is not on the IRS's radar screen, at least ostensibly? There are consequences for failing to file an income tax return, and the IRS seems to be a forgiving mood considering the People First Initiative and other guidance issued during the COVID-19 pandemic.

First, the non-filer could be charged with a crime. The willful failure to file a tax return is a misdemeanor under Section 7203 of the Internal Revenue Code (Code). Generally, the Criminal Investigation Division of the IRS and its Special Agents are looking for a pattern of multiple and consecutive years of non-filing – three years or more. Professional persons and other prominent persons in the community are especially at risk. Substantial unreported income also plays a major role regardless of the person's profession or prominence in the community. Where, however, there are overt acts of attempted evasion, for example: dealing in cash, hiding or concealing assets, or transferring income-producing assets to family members or nominees to avoid detection, the willful failure to file could be elevated to a felony under Section 7201 of the Code. In either case, if convicted, the punishment could include prison time and substantial fines. A claim by the non-filer that he/she did not know that returns needed to be filed will not wash. What the non-filer doesn't want to do is to turn a **civil case** for failing to file returns into a **criminal case by continuing to be dilatory and not addressing the issue** – the repercussions are too severe.

Second, there are **civil penalties** for such failures – late filing penalties up to a maximum of 25% of the unpaid tax (Section 6651(a)(1)); late paying penalties up to a maximum of 25% of the unpaid tax (Section 6651(a)(2)); failure to pay estimated tax penalty under Section 6654; and the potential for a fraudulent failure to file penalty under Section 6651(f) of 75% of the unpaid tax.

Third, **there is no statute of limitations if the non-filer fails to file a return in accordance with the provisions of Section 6501(c)(3)**. The statute of limitations on assessment and collection of taxes does not start or begin to run until a return is filed by the taxpayer (Section 6501(a)) or on his behalf by the IRS from third-party information such as Forms W-2 and 1099 and other steps are taken by the IRS with respect to this substitute for return procedure under Section 6201. Consequently, the IRS can assess and collect taxes for the unfiled years **at any time**, many years later, even after the death of the non-filer, which is sometimes the case. Unfortunately, the surviving family members must deal with the non-filer's delinquencies and the reconstruction of those returns may become problematic due to the lack of records.

Lastly, and as previously eluded to, the statute of limitations on refunds is three years from the due date of the return for the year involved or two years from the time the tax was paid, whichever expires later. Thus, absent the current automatic extension to July 15 under Notice 2020-23, the statute of limitations for the 2016 has already expired as the filing date was April 15, 2017 and three-year period would have expired on April 15, 2020, absent a valid extension to file said return. Section 6511(b)(2)(A). Thus, any refund related return for 2016 must be filed on or before July 15, 2020. The statute of limitations for refunds due for 2015 and earlier years has already expired.

We have helped many non-filers over the years and are currently assisting more non-filers with the IRS and the state taxing authorities. We can also assist in finding a competent tax return preparer, such as a certified public accountant (CPA), and work with them for purposes of compliance and any subsequent determinations by the IRS or state taxing authorities. As noted above, the time is ripe to become compliant with any IRS filing obligations. The delinquency issue is not going to fade away; it can only get worse with further procrastination.

For more information and guidance, or if you just have some questions concerning your filing obligations, please reach-out to Nexsen Pruet attorneys Paul G. Topolka at 336.387.5123 or David M. McCallum at 919.573.7440.

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